

VZCZCXRO2613
RR RUEHCHI RUEHCN RUEHDT RUEHGH RUEHHM RUEHNH
DE RUEHGZ #0033/01 0200710
ZNR UUUUU ZZH
R 200710Z JAN 10
FM AMCONSUL GUANGZHOU
TO RUEHC/SECSTATE WASHDC 1305
INFO RUEHOO/CHINA POSTS COLLECTIVE 0439
RUCNASE/ASEAN MEMBER COLLECTIVE
RUEHBJ/AMEMBASSY BEIJING 1062
RUEHCN/AMCONSUL CHENGDU 0365
RUEHHK/AMCONSUL HONG KONG 0428
RUEHGH/AMCONSUL SHANGHAI 0364
RUEHSH/AMCONSUL SHENYANG 0374
RUCPDO/DEPT OF COMMERCE WASHDC
RUEATRS/DEPT OF TREASURY WASH DC
RUEHC/DEPT OF LABOR WASHDC
RUEAIIA/CIA WASHDC 0407
RUEKJCS/DIA WASHDC 0403

UNCLAS SECTION 01 OF 03 GUANGZHOU 000033

SENSITIVE
SIPDIS

STATE FOR EAP/CM, EAP/EP, EEB/TPP, EEB/IFD, S/P, INR/EAP
STATE PASS USTR CHINA OFFICE

E.O. 12958: N/A

TAGS: [ETRD](#) [ECON](#) [EFIN](#) [EINV](#) [PGOV](#) [CH](#) [HK](#)

SUBJECT: CHINA-HONG KONG: CEPA IMPLEMENTATION IN GUANGDONG NOT
ACCELERATING SERVICE SECTOR LIBERALIZATION

REF: A) 09 HONG KONG 1898; B) 09 HONG KONG 1847

GUANGZHOU 00000033 001.2 OF 003

(U) This document is sensitive but unclassified. Please protect accordingly. Not for release outside U.S. government channels. Not for internet publication.

¶1. (SBU) Summary and comment: Numerous barriers continue to hinder service sector liberalization as envisioned by the Beijing-Hong Kong Closer Economic Partnership Agreement's (CEPA) sixth supplemental agreement that took effect on October 1, 2009, according to Guangzhou-based contacts in meetings with Guangzhou and Hong Kong econoffs. Obstacles range from industry-specific barriers related to licensing and local protectionism to general structural weaknesses in local business rules and ineffective enforcement of CEPA 6 through weak local offices of China's Ministry of Commerce (MOFCOM). At the same time, contacts said the influx of Hong Kong banks into China surged in 2009 and could be expected to continue expanding in 2010, but this change had little to do with implementation of the latest CEPA agreement and was mostly based on unilateral mainland easing of previous restrictions. In other fields, like accounting, contacts went further and expressed ambivalence about cross-border business opportunities. Contacts said the local market is attractive enough that Guangzhou accountants and many lawyers are uninterested in possible expansion that would lead into Hong Kong's market. Without increased focus on these obstacles at the local level, it appears that generous praise for the concept of CEPA 6 advancing mainland-Hong Kong service sector integration will continue to ring hollow in south China. End summary and comment.

Local Barriers Continue

¶2. (SBU) Guangzhou-based Director Ronald Ho of the Hong Kong Trade and Development Council (HKTDC) told Guangzhou and Hong Kong econoffs in a December joint meeting that although the CEPA 6 services agreement between Hong Kong and Beijing is an important step towards greater economic integration, significant barriers remain before the service industry can operate on both sides of the border in the spirit of the agreement. Ho said industry-specific barriers remain in areas throughout Guangdong Province for many service sectors, including medicine, law, and architecture, mostly

in the form of insurmountable obstacles for Hong Kong individuals and firms to acquire local operating licenses (ref A).

13. (SBU) The license problem is a combination of local officials who lack understanding of their responsibilities under the CEPA agreements, coupled with resistance from local service sector businesses which often feel threatened by the possible entrance of new Hong Kong competitors to their markets; they resort to local protectionism, according to Ho. In the case of education services, resistance from local officials in many areas of Guangdong Province is more direct, as they fear "brain drain" if Hong Kong Universities are allowed to recruit mainland students without any sort of administrative backstop. Ho further explained that two types of obstacles had sprung up in the education sector, one direct and one indirect: Hong Kong Universities and other institutes of higher education are seldom allowed to participate in local education fairs in Guangdong Province, and students are forced to take an all-or-nothing approach because the testing deadlines for Hong Kong and the mainland are out of sync. Thus, students are unable to weigh their options and make a balanced choice after the testing results become available.

Structural Weaknesses Also Inhibit CEPA

14. (SBU) HKTDC Director Ho pointed to general structural weaknesses in the mainland administrative system that also hinder full implementation of CEPA 6 commitments on service sector integration. Outdated and counter-intuitive local bureaucratic processes in many areas of Guangdong Province inhibit the ability of modern service industries from taking root. One example Ho cited was a Hong Kong-owned convenience store chain that would like to open 1,000 new stores in and around Foshan City, but tax and jurisdictional rules restrict individual stores from registering as branches of a single

GUANGZHOU 00000033 002.2 OF 003

business entity. Basic supply operations to efficiently balance inventories among different stores would trigger taxable transactions whenever unsold goods are moved between stores in different parts of the city, cancelling out the effects of modern inventory control and making the business too costly for a new entrant to the market. Ho speculated that as China's responsible agency for the CEPA agreement, local representatives of MOFCOM should be able to help local officials revise regulations and better comply with Beijing's CEPA obligations, but he said the agency's local branches are relatively weak in comparison to other elements of local government, meaning that resolution at the local level is difficult, if not impossible.

Cross-Border Banking Expanded Regardless of CEPA

15. (SBU) Hong Kong is more excited about CEPA than people in mainland China, according to Guangzhou Branch President Lin Chunxiang of China Mercantile Bank, a wholly-owned subsidiary of the Industrial and Commercial Bank of China (ICBC). Lin said China Mercantile was established in Shenzhen in 1993, and operates with both onshore and offshore banking licenses in China, specifically catering to ICBC banking clients on both sides of the Hong Kong-mainland border. Lin told econoffs that Hong Kong banks expanded quickly into Guangdong Province in 2009 due to long-term reforms in mainland banking regulations, a trend he expects to continue in 2010, but that the rapid expansion does not threaten ICBC's banking businesses on either side of the border because loyalty of the bank's customers remains high and the Guangdong market is growing rapidly enough for each bank to enjoy success.

Guangzhou Accountants: Do We Need CEPA?

16. (SBU) According to Secretary General Jiang Jianping of the Guangzhou Institute of Certified Public Accountants (GICPA), the "Big 4" international accounting firms have worked in the mainland since the 1980's and setup their first official offices starting in 2000, long before the initial CEPA agreement between Beijing and Hong Kong. Jiang told econoffs that the Big 4 accounting firms

enjoy a market share of almost 50% in Guangzhou, with small- and medium-sized firms handling the remaining smaller and less international clients.

17. (SBU) Jiang commented that with each of the Big 4 firms tightly bound to a local partner and the Guangzhou accounting market already very mature, new competition from Hong Kong-based firms appears unlikely in the near or medium term. When asked about mainland accounting firms entering the Hong Kong market, Jiang said that a successful strategy would be to grow with its major customers and establish branches overseas as customer requirements expand. However, Jiang cited the example of a mainland accounting firm that failed in its effort to penetrate the Hong Kong market and expressed doubt the new CEPA agreement would lead accounting firms to take this risk, especially when the local demand for accounting services continued to expand.

Some Lawyers Break Mold and Cross the Border

18. (SBU) Junius Ho of Hong Kong-based K.C. Ho & Fong Law Firm told econoffs his representative office in Guangzhou was unique as a Hong Kong firm that has setup an office in Guangdong Province. The firm's one-year-old offices in downtown Guangzhou are co-located with Right Word Law Firm (Guangdong), and licensed lawyers from both jurisdictions work together to support clients in both Hong Kong and Mainland China. Ho expressed optimism for his firm's first-to-market strategy but was reluctant to offer estimates of how long it would take for the rest of the legal market to follow his firm's example. As Director Rex Chang of the Hong Kong Economic and Trade Office in Guangdong separately told econoffs, early CEPA agreements already liberalized trade in goods, and manufacturing is never going to return to Hong Kong, making the service sector the only remaining area for economic integration. Integration will face challenges and take time, but this is the future and issues will be resolved over time, he said.

GUANGZHOU 00000033 003.2 OF 003

19. (SBU) Consulate General Hong Kong has cleared this joint reporting cable.

GOLDBECK